



COMMONWEALTH HEALTH INSURANCE CONNECTOR AUTHORITY

(A Component Unit of the Commonwealth of Massachusetts)

Financial Statements and Required Supplementary Information

June 30, 2019

(With Independent Auditors' Report Thereon)



KPMG LLP
Two Financial Center
60 South Street
Boston, MA 02111

Independent Auditors' Report

The Board of Directors
Commonwealth Health Insurance Connector Authority:

Report on the Financial Statements

We have audited the accompanying financial statements of the Commonwealth Health Insurance Connector Authority (the Health Connector), a component unit of the Commonwealth of Massachusetts, which comprise the Statements of Net Position, Revenues, Expenses, and Changes in Net Position and Cash Flows as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Health Connector's basic financial statements for the year then ended.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles (GAAP); this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Commonwealth Health Insurance Connector Authority as of June 30, 2019, and the changes in its financial position and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.



Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the Management's Discussion and Analysis on pages 3–7 and the Schedule of Proportionate Share of Net Pension Liability on page 22, and the Schedule of Changes in Total OPEB Liability and Related Ratios on page 23, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 1, 2019, on our consideration of the Health Connector's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Health Connector's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Health Connector's internal control over financial reporting and compliance.

KPMG LLP

Boston, Massachusetts
November 1, 2019

COMMONWEALTH HEALTH INSURANCE CONNECTOR AUTHORITY
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Management's Discussion and Analysis – Unaudited

June 30, 2019

Introduction

The following discussion of the financial performance and activity of the Commonwealth Health Insurance Connector Authority (the Health Connector) is intended to provide an overview and analysis of the basic financial statements for the fiscal year ended June 30, 2019. The management of the Health Connector has prepared this discussion and it should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Background of the Health Connector

The Health Connector is a body politic and a corporate and public instrumentality of the Commonwealth of Massachusetts (the Commonwealth). The Health Connector is established pursuant to Chapter 176Q of the Massachusetts General Laws (MGLs) and is an independent public entity not subject to the supervision and control of any other office, department, commission, board, bureau, agency or political subdivision of the Commonwealth.

The Health Connector is governed by an eleven member public private Board, comprised of four ex-officio members – the Secretary of the Executive Office of Health and Human Services (EOHHS), who serves as chair of the Board; the Secretary of Administration and Finance; the Executive Director of the Group Insurance Commission (GIC); and the Commissioner of Insurance, as well as seven members of the public, four appointed by the Governor and three appointed by the Attorney General. Public sector members encompass a range of interests and expertise, including organized labor, employee health benefits, consumers, small business, actuarial science, health economics and health insurance brokerage.

The Health Connector's primary responsibility is to facilitate the availability, choice and adoption of private health insurance plans to eligible individuals and small businesses. Since January 1, 2014, the Health Connector has operated as a State-Based Marketplace (SBM) that meets the requirements of the Affordable Care Act (ACA). The Health Connector currently offers the following programs:

- Qualified Health Plans (QHPs) and Qualified Dental Plans (QDPs) for eligible individuals. Individuals with income up to 400% FPL may be eligible for federal Advanced Premium Tax Credits (APTC).
- ConnectorCare is a subsidized health insurance program offering QHPs to individuals at 300% or less of the FPL. In addition to federal tax credits, ConnectorCare members also receive state subsidies (state premium wrap and cost sharing reductions) to further offset premium and point-of-service costs.
- Health Connector for Business (previously Small Business Health Options Program or SHOP) offers QHPs and QDPs to small businesses. Small businesses may be eligible for ACA small business tax credits up to 50% of the cost of health insurance for businesses with fewer than 25 full time equivalent employees, who earn on average \$50,000 a year or less in 2019.
- The Navigator program is required by the ACA and provides grants to community organizations that assist consumers (individuals, families and small businesses), using culturally and linguistically appropriate methods, to learn about their health care coverage options; access any applicable federal tax credits and other state subsidies; and enroll in a health plan.
- The Wellness Track program, established by Chapter 288 of the Acts of 2010, which allows eligible employers to earn up to a 15% rebate on the premium contribution for promoting a healthy workforce.

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In addition, the Health Connector continues to be responsible for, among other things, policy development relative to the Affordability Schedule and Minimum Credible Coverage rules; administration of appeals filed on behalf of individuals in accordance with ConnectorCare program regulations and the Commonwealth's individual mandate; and public education and outreach activities.

Health Connector Operations

As of June 30, 2019, the Health Connector employed approximately 73 full-time equivalent personnel in business administration and program functions (i.e., finance, legal, operations, policy, outreach, plan management and information technology or IT), as well as support functions, including an appeals unit to manage the appeals process for the individual mandate and ConnectorCare eligibility determinations. Additionally, the Health Connector subcontracts a significant amount of back office operations to public entities and private vendors, primarily IT development and maintenance and customer service and business operations.

Current Year Activities

In FY2019, the Health Connector continued to operate ACA-required programs that launched on January 1, 2014. Many key accomplishments were achieved during FY2019, most notably a successful 2019 Open Enrollment that provided a stable customer experience for both new and renewing members. As of June 2019, there were over 286,140 individuals enrolled in QHPs and 6,598 small group QHPs. In addition, 96,927 of our QHP members were also enrolled in QDPs or were members with a dental only policy.

A key activity in FY2019, the Customer Experience Project (CXP) culminated in the selection of new vendors to perform enrollment, premium billing, member portal, contact center, walk-in centers, noticing and mailroom functions that are currently performed by NTT Data for our nongroup population. The current contract with NTT Data expires on June 30, 2020 so an internal team was launched in 2017 to create a strategy and path for procurement.

On April 11, 2019, the Health Connector Board of Directors voted to enter into an agreement with Softheon, Inc. to perform enrollment, premium billing, noticing and member portal services beginning April 12, 2019 through June 30, 2024, with two, two-year renewal options. Softheon will go-live and begin serving our members on June 1, 2020.

On August 19, 2019, the Health Connector Board of Directors voted to enter into an agreement with Faneuil, Inc. to perform contact center, back office and walk-in services beginning August 20, 2019 through June 30, 2024, with two, two-year renewal options. Faneuil will go-live and begin serving our members on June 1, 2020.

The Financial Statements

The Health Connector's financial report includes three financial statements: the Statement of Net Position (similar to a balance sheet); the Statement of Revenues, Expenses and Changes in Net Position; and the Statement of Cash Flows. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as promulgated by the GASB. Under this method of accounting, an economic resources measurement focus and an accrual basis of accounting is used, similar to private industry. Revenue is recorded when earned, and expenses are recorded when incurred.

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Management's Discussion and Analysis – Unaudited

June 30, 2019

The Statement of Net Position presents information on the Health Connector's Total Assets and Deferred Outflows and Total Liabilities and Deferred Inflows, with the difference between the two reported as Net Position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Health Connector is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Position reports the operating revenues and expenses and nonoperating revenues and expenses of the Health Connector for the fiscal year. The difference – increase or decrease in net position – is presented as the change in net position for the fiscal year. The cumulative differences from inception forward are presented as the net position of the Health Connector, reconciling to total net position on the Statement of Net Position.

The Statement of Cash Flows presents information showing how the Health Connector's cash and cash equivalents position changed during the fiscal year. The Statement of Cash Flows classifies cash receipts and cash payments as resulting from operating activities, capital and related financing activities, noncapital financing activities and investing activities. The net result of those activities is reconciled to the cash and short-term investment balances reported at the end of the fiscal year. This statement is prepared using the direct method, which allows the reader to easily understand the amount of cash received and how much cash was disbursed.

Summarized Financial Information

Summarized financial information as of and for the years ended June 30, 2019 and 2018 is as follows:

Table 1

Net Position

(In thousands)

	<u>2019</u>	<u>2018</u>
Current assets	\$ 113,386	88,618
Capital assets	<u>1,737</u>	<u>246</u>
Total assets and deferred outflows	\$ <u>115,123</u>	<u>88,864</u>

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Management's Discussion and Analysis – Unaudited

June 30, 2019

Table 1
Net Position
(In thousands)

	<u>2019</u>	<u>2018</u>
Current liabilities	\$ 70,255	58,384
Long term liabilities	6,177	5,602
Deferred inflows of resources	<u>3,499</u>	<u>3,446</u>
Total liabilities and deferred inflows	\$ <u>79,931</u>	<u>67,432</u>
Net position:		
Invested in capital assets	\$ 1,737	246
Unrestricted	<u>33,455</u>	<u>21,186</u>
Total net position	\$ <u>35,192</u>	<u>21,432</u>

Table 2
Changes in Net Position
(In thousands)

	<u>2019</u>	<u>2018</u>
Operating revenues	\$ 838,023	771,985 (1)
Operating expenses	<u>872,639</u>	<u>815,284 (1)</u>
Operating loss	(34,616)	(43,299)
Nonoperating revenue	<u>48,376</u>	<u>49,780</u>
Increase in net position	\$ <u>13,760</u>	<u>6,481</u>

(1) Prior year operating revenue and expenses were restated to include amounts related to the small business program for approximately \$26 million.

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Management's Discussion and Analysis – Unaudited

June 30, 2019

Financial Highlights

For FY2019, the Health Connector had a net operating loss of \$34,616,238 on operating revenues of \$838,022,784 and operating expenses of \$872,639,022.

Operating revenues include \$465,925,280 in premiums billed to QHP and QDP enrollees. Premiums for QHP and QDP enrollees are billed one month in advance of the coverage period. Premium payments collected by the Health Connector from QHP and QDP enrollees are paid to the carriers on a monthly basis. Additional FY2019 operating revenues include state-funded premium subsidies and cost sharing reduction subsidies, which were \$151,096,470 and \$147,744,648, respectively. Both subsidies, which are part of the Health Connector's ConnectorCare program, supplement federal subsidies to further strengthen affordability of coverage for individuals with income at or below 300% of the FPL. These subsidies, which are funded from the Commonwealth Care Trust Fund (CCTF), are paid to the carriers on a monthly basis. The CCTF is a fund that is managed and administered by the Commonwealth.

FY2019 operating revenue also includes \$31,628,648 in premiums billed to Health Connector for Business (HCB) employers. Premiums for HCB employers are billed one month in advance of the coverage period. Premium payments collected by the Health Connector from HCB employers are paid to the carriers on a monthly basis.

Additional FY2019 operating revenue includes \$36,300,449, of administrative fees assessed to the carriers. The administrative fee assessed to the carriers for ConnectorCare QHP enrollees is 3.0% of the sum of enrollee premiums paid, federal APTC and state premium subsidies paid to the carriers. The administrative fee assessed to the carriers for non-ConnectorCare QHP enrollees is 2.5% of the sum of enrollee premiums paid and federal APTC. The administrative fee assessed to the carriers for QDP enrollees is 3.0% of the enrollee premiums paid. Nonoperating revenue, includes other grant revenue of \$117,060, a CCTF contribution for administrative operations of \$45,000,000, intergovernmental revenue of \$2,040,588 and investment income of \$1,218,252.

In FY2019, the Health Connector capitalized \$1,597,598 in costs related to the development of internally generated software. These costs include \$987,436 for services provided by Softheon, Inc., \$451,163 for Health Connector staff costs, and \$158,999 for consulting services.

Contacting the Health Connector's Management

This financial report is designed to provide citizens, taxpayers and creditors with a general view of the Health Connector's finances and to show the Health Connector's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact Kari Miller, Chief Financial Officer, Commonwealth Health Insurance Connector Authority at 100 City Hall Plaza, 6th Floor, Boston, MA 02108.

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Statement of Net Position

June 30, 2019

Assets and Deferred Outflows

Current assets:	
Cash and short-term investments (note 2)	\$ 98,971,519
Accounts receivable:	
Qualified Health and Dental plan enrollees, net (note 3)	10,104,137
Nonfederal grants	48,480
Other assets	<u>4,261,511</u>
Total current assets	113,385,647
Noncurrent assets:	
Capital assets, net (note 10)	<u>1,737,508</u>
Total assets and deferred outflows	<u>115,123,155</u>

Liabilities and Deferred Inflows

Current liabilities:	
Accounts payable	272,196
Accounts payable – carriers (note 6)	2,590,510
Unearned revenue (note 4)	44,850,530
Accrued salary and benefits	693,590
Accounts payable – enrollee overpayments	6,060,662
Due to Commonwealth (note 5)	9,774,898
Other liabilities	<u>6,012,813</u>
Total current liabilities	<u>70,255,199</u>
Long term liabilities:	
OPEB obligation (note 8)	<u>6,176,965</u>
Total long term liabilities	<u>6,176,965</u>
Deferred inflows of resources:	
Deferred inflows related to OPEB	<u>3,498,883</u>
Total deferred inflows of resources	<u>3,498,883</u>
Total liabilities and deferred inflows	<u>79,931,047</u>

Net Position

Net position:	
Invested in capital assets	1,737,508
Unrestricted	33,454,600
Commitments and contingencies (note 9 and 12)	
Total net position	<u>\$ 35,192,108</u>

See accompanying notes to financial statements.

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Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2019

Operating revenues:	
Qualified health and dental plan enrollee premiums	\$ 465,925,280
Health Connector for Business enrollee premiums	31,628,648
State wrap premium subsidy – ConnectorCare	151,096,470
State cost sharing reduction subsidy – ConnectorCare	147,744,648
State Mandated Benefits	205,929
State funded federal replacement cost sharing reduction subsidy (note 11)	(1,853,425)
Carrier Administrative fees	36,300,449
Medical loss ratio rebate	6,426,278
Other revenue	<u>548,507</u>
Total operating revenues	<u>838,022,784</u>
Operating expenses:	
Carrier payments – qualified health and dental plan enrollee premiums	465,925,280
Carrier payments – Health Connector for Business enrollee premiums	31,628,648
State wrap premium subsidy – ConnectorCare	151,096,470
State cost sharing reduction subsidy – ConnectorCare	147,744,648
State Mandated Benefits	205,929
State funded federal replacement cost sharing reduction subsidy (note 11)	(1,853,425)
Consulting and professional support	1,339,545
Customer service and premium billing	45,977,828
Navigator program	1,805,066
Salaries, benefits, and payroll taxes	7,676,550
Communications	2,856,484
General and administrative	250,456
IT and communications	7,277,107
Facility and related	919,696
Depreciation expense	106,330
Program appeals	238,678
Postemployment expense (notes 7 and 8)	2,679,241
Medical loss ratio rebate	6,426,278
Customer experience project	99,622
Wellness track subsidies	<u>238,591</u>
Total operating expenses	<u>872,639,022</u>
Operating loss	<u>(34,616,238)</u>
Nonoperating revenue:	
CCTF contributions	45,000,000
Intergovernmental revenue (note 7)	2,040,588
Investment income	1,218,252
Other grant revenue	<u>117,060</u>
Total nonoperating revenue	<u>48,375,900</u>
Increase in net position	13,759,662
Net position – beginning of fiscal year	<u>21,432,446</u>
Net position – end of fiscal year	<u>\$ 35,192,108</u>

See accompanying notes to financial statements.

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Statement of Cash Flows

Year ended June 30, 2019

Cash flows from operating activities:	
Cash paid to employees	\$ (4,169,643)
Cash paid to vendors	(69,756,659)
Cash refunds paid to enrollees	(10,696,413)
Cash received from Commonwealth	318,159,731
Cash paid to carriers	(759,404,380)
Cash paid to carriers (HCB)	(30,578,378)
Cash received from qualified health and dental plan enrollees	476,556,406
Cash received from Health Connector for Business enrollees	32,915,168
Cash refunds paid to Health Connector for Business enrollees	(101,483)
Cash received from health plans (MLR rebates)	2,674,853
Cash paid to Commonwealth (MLR rebates)	(2,674,853)
Operating revenue:	
Administrative fees	36,300,323
RADV user fee	583,771
Other	<u>244,197</u>
Net cash used for operating activities	<u>(9,947,360)</u>
Cash flows from capital and related financing activities:	
Cash received from nonfederal grants	72,405
Purchase of capital assets	<u>(1,059,953)</u>
Net cash provided by capital and related financing activities	<u>(987,548)</u>
Cash flows from noncapital and related financing activities:	
Cash received from Commonwealth (CCTF contributions)	<u>48,750,000</u>
Net cash provided by noncapital and related financing activities	<u>48,750,000</u>
Cash flow from investing activities:	
Investment earnings	<u>1,218,252</u>
Net cash provided by investing activities	<u>1,218,252</u>
Net increase in cash and short-term investments	39,033,344
Cash and short-term investments at the beginning of the fiscal year	<u>59,938,175</u>
Cash and short-term investments at the end of the fiscal year	<u>\$ 98,971,519</u>
Reconciliation of operating loss to cash used for operating activities:	
Operating loss	\$ (34,616,238)
Adjustments to reconcile operating loss to cash used for operating activities:	
Depreciation	106,330
Intergovernmental expense	2,040,588
Changes in operating assets and liabilities:	
Decrease in nonfederal/nonCCTF receivables	14,553,154
Increase in other assets	(3,992,592)
Increase in accounts payable, and accrued liabilities	11,333,574
Increase in OPEB liability, net	<u>627,824</u>
Net cash used for operating activities	<u>\$ (9,947,360)</u>
Non-cash capital and related financing activities:	
Noncash capital acquisitions	\$ 537,645

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Notes to Financial Statements

June 30, 2019

(1) Summary of Significant Accounting Policies

(a) Reporting Entity

The Health Connector is an independent body politic and corporate and public health instrumentality of the Commonwealth of Massachusetts established pursuant to Chapter 176Q of the Massachusetts General Laws (MGLs) as added by Section 101 of Chapter 58 of the Acts of 2006.

Due to its relationship with the Commonwealth, the Health Connector is considered a discretely presented component unit and is presented as such in the Commonwealth's financial statements. The Health Connector has no relationship with other entities that could be considered component units. The Connector is exempt from Federal, State, and local income taxes.

(b) Basis of Presentation

The accompanying financial statements of the Health Connector have been prepared in accordance with U.S. GAAP, as prescribed by the Governmental Accounting Standards Board (GASB). The Health Connector has prepared a "Statement of Net Position," a "Statement of Revenues, Expenses and Changes in Net Position" and a "Statement of Cash Flows," along with the required supplementary information titled "Management's Discussion and Analysis" which precedes the financial statements and the required supplementary schedules titled "Schedule of Proportionate Share of Net Pension Liability" and "Schedule of Changes in Total OPEB Liability and Related Ratios".

The Health Connector utilizes the full accrual basis of accounting, which focuses on changes in total economic resources, in the preparation of financial statements. Under the full accrual basis of accounting, long term assets and liabilities are reflected in the financial statements.

(c) Cash and Cash Equivalents

The Health Connector considers all highly liquid investments with an original maturity of 30 days or less when purchased to be cash equivalents.

(d) Investments

The Health Connector is authorized to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bonds or notes of public agencies or municipalities, bank time deposits, guaranteed investment contracts, money market accounts including money market like instruments such as the Massachusetts Municipal Depository Trust (MMDT), and repurchase agreements. Investments other than MMDT are recorded at fair value. MMDT is valued at its net asset value (NAV) or \$1.00 per share. MMDT is an external investment pool overseen by the Massachusetts State Treasurer.

At June 30, 2019, investments consist entirely of amounts held in MMDT.

(e) Capital Assets

The Health Connector defines capital assets as classes of assets with an initial aggregate cost of more than \$49,999 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed.

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Notes to Financial Statements

June 30, 2019

(f) Depreciation

Depreciation is calculated on the straight-line method based on the estimated useful lives of between three and 10 years for the applicable assets beginning in the fiscal year of acquisition.

(g) Revenue Recognition

The Health Connector recognizes revenue when earned. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

The Health Connector's major operating revenue sources are Qualified Health Plan (QHP) and Qualified Dental Plan (QDP) enrollee contributions, Health Connector for Business enrollee contributions, ConnectorCare state wrap premium and cost sharing reduction subsidies, and administrative fees collected from the carriers. The state wrap and cost sharing reduction subsidies, which are part of the Health Connector's ConnectorCare program, supplement federal subsidies to further strengthen affordability of coverage for individuals with income at or below 300% of the FPL.

Other grant revenue, intergovernmental revenue and investment income are reported as nonoperating revenues. Also reported in nonoperating revenues are contributions from the Commonwealth Care Trust Fund (CCTF) to support the Health Connector's operations.

Operating expenses include QHP and QDP enrollee premiums billed and collected by the Health Connector and paid to the carriers. Operating expenses also include state-funded premium and cost sharing reduction subsidies received from the CCTF and paid to the carriers. In addition, the Health Connector includes as operating expenses payments for customer service and business operations, the Navigator program, the Appeals program, outreach, personnel and other administrative items.

(h) Compensated Absences and Other Employee Benefits

Employees earn the right to be compensated during absences for vacation, personal and sick time (earned time or ET). Upon retirement, termination or death, certain employees are compensated for ET (subject to certain limitations) at their then current rate of pay. Accumulated ET is recorded as an expense and liability as benefits accrue. As of June 30, 2019, the ET liability was \$552,172.

The employees of the Health Connector participate in the Commonwealth's Group Insurance Commission (GIC) for all healthcare benefits except for dental and vision benefits, which are purchased directly through Delta Dental and Vision Service Plan.

(i) Deferred Outflows of Resources and Deferred Inflows of Resources

Deferred outflows of resources are defined as a consumption of net assets that is applicable to a future reporting period. Deferred inflows of resources are defined as an acquisition of net assets that is applicable to a future reporting period. Deferred outflows of resources increase net position, similar to assets, whereas deferred inflows of resources decrease net position, similar to liabilities.

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(j) Retirement Plan

For purposes of measuring the net pension liability and pension expense, information about the fiduciary net position of the Massachusetts State Employees Retirement System (SERS) and additions to/deductions from SERS's fiduciary net position have been determined on the same basis as they are reported by SERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investment of assets in the SERS is with the Pension Reserves Investment Trust (PRIT) Fund, which is managed by the Pension Reserves Investment Management (PRIM) Board. The PRIM Board seeks to maximize the total return on investments within acceptable levels of risk for public pension funds. Investments are reported at fair value as described in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Massachusetts.

(k) Use of Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) Cash and Investments

Deposits with Financial Institutions

Custodial credit risk is the risk that, in the event of the failure of a depository financial institution, the depositor will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. Deposits are exposed to custodial credit risk if they are large uninsured deposits with no collateral agreements.

As of June 30, 2019, the Health Connector had bank deposits of \$49,259,081 that exceeded the Federal Deposit Insurance Corporation (FDIC) coverage of \$250,000.

As of June 30, 2019, the Health Connector had bank deposits of \$3,907,170 that are fully collateralized per the Tri-Party Collateral agreement between the Health Connector, Wells Fargo Bank, N.A., and the Bank of New York Mellon.

Investments

The Health Connector's investment policy is to ensure that cash is invested in a stable investment option with consistent and competitive yields. As of June 30, 2019, available cash is invested in the MMDT Cash Portfolio option.

MMDT's average maturity is less than a year and not-rated for risk purposes. The Health Connector's position in MMDT as of June 30, 2019 was \$51,130,012 and is classified as part of cash and short-term investments.

(3) Accounts Receivable – Qualified Health and Dental Plan Enrollees

As of June 30, 2019, the unpaid portion of the health insurance premium billed to QHP and QDP enrollees was \$21,836,618. The allowance for uncollectible accounts receivable at June 30, 2019 was \$11,732,481.

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Notes to Financial Statements

June 30, 2019

(4) Unearned Revenue

As of June 30, 2019, the Health Connector had \$44,850,530 in unearned revenue for QHP and QDP enrollees whose premiums are billed one month in advance of the coverage month.

(5) Due to Commonwealth

As of June 30, 2019, the amount due to the Commonwealth was \$9,774,898. The FY2019 amount due to the Commonwealth includes \$6,588 in IT chargebacks, \$3,751,425 in Tufts Health Plans' benefit year 2018 Medical Loss Ratio (MLR) rebates and \$6,104,000 which represents the Health Connector's share of the Health Insurance Exchange Integrated Eligibility System (HIX-IES) operations and maintenance costs incurred under the Optum contract, managed by EOHHS. These amounts are offset by \$87,115 which represents the FY2017 Cost Sharing Reduction (CSR) receivable for Celticare.

(6) Accounts Payable – Carriers

As of June 30, 2019, the amount due to the carriers was \$2,590,510 which represents QHP and QDP subscriber premium payments owed to the Carriers.

(7) Retirement Plan

(a) Plan Description

All eligible employees of the Health Connector are provided with pension benefits through the Massachusetts SERS, a cost-sharing multiple-employer defined benefit pension plan administered by the Massachusetts State Retirement Board. SERS does not issue a stand-alone publicly available financial report, but its activities are included in a pension trust fund in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Massachusetts.

(b) Benefits Provided

SERS provides retirement, disability, survivor and death benefits to members and their beneficiaries. The MGLs establishes the benefit and contribution requirements for SERS. These requirements provide for superannuation retirement allowance benefits up to a maximum of 80% of a member's highest three-year average annual rate of regular compensation. For employees hired after April 1, 2012, retirement allowances are calculated on the basis of the last five years of consecutive years, whichever is greater in terms of compensation? Benefit payments are based upon a member's age, length of creditable service, group creditable service, and group classification. The authority for amending these provisions rests with the Legislature.

Members become vested after ten years of creditable service. A superannuation retirement allowance may be received upon the completion of twenty years of service or upon reaching the age of 55 with ten years of service. Normal retirement for most employees occurs at the age of 65; for certain hazardous duty and public safety positions, normal retirement is at the age of 55. Most employees who joined the system after April 1, 2012 cannot retire prior to age 60. The retirement systems' funding policies have been established by Chapter 32 of the MGL. The Legislature has the authority to amend these policies. The annuity portion of the SERS retirement allowance is funded by employees, who contribute a percentage of their regular compensation. Costs of administering the plan are funded out of plan assets.

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(c) Contributions

SERS funding policies have been established by Chapter 32 of the MGL. The Legislature has the authority to amend these policies. Member contributions for SERS vary depending on the most recent date of membership from 5% regular compensation for hires prior to 1975 to 11% of regular compensation for hire dates after July 1, 2001. For members hired after 1979, an additional contribution of 2% of regular compensation in excess of \$30,000 is also required.

(i) Pension Liabilities and Pension Expense

At June 30, 2019, the Health Connector was allocated a liability of \$15,489,168 for its proportionate share of the net pension liability of SERS but was not required to record this liability as the Commonwealth is legally responsible for paying the liability.

The Commonwealth is legally responsible to make employer contributions related to the Health Connector's employees participating in SERS. As such, the Commonwealth has a 100% special funding situation for the Health Connector. Accordingly, the Health Connector recognized \$2,040,588 as pension expense and intergovernmental revenue of the same amount in the statement of revenues, expenses and changes in net position for the year ended June 30, 2019.

Health Connector's proportionate share of the net pension liability	\$	—
Commonwealth's proportionate share for the net pension liability associated with the Health Connector		15,489,168
Total	\$	15,489,168

The net pension liability was measured as of June 30, 2018 (the Measurement Date), and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of January 1, 2018 and rolled forward to the Measurement Date. The Health Connector's proportion of the net pension liability was based on allocated nonemployer contributions. At June 30, 2018, the Health Connector's proportion was 0.11708% which was an increase of 0.54% from its proportion of 0.11645% measured as of June 30, 2017.

(d) Actuarial Assumptions

The total pension liability in the January 1, 2018 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement.

- Salary increases: 4.0% to 9.0% depending on the group and length of service
- Investment rate of return: 7.35% net of pension plan investment expense, including inflation; 3.5% interest rate credited to the annuity savings fund
- Cost of living increase: 3.0% per year

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Mortality rates were based on the following:

- Pre-retirement – reflects RP 2014 Blue Collar Employees Table projected generationally with Scale MP-2016 and set forward 1 year for females
- Post-retirement – reflects RP 2014 Blue Collar Healthy Annuitant Table projected generationally with Scale MP-2016 set forward 1 year for females
- Disability – the mortality rate reflects RP-2014 Blue Collar Healthy Annuitant Table projected generationally with Scale MP-2016 set forward 1 year

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future rates of return by the target asset allocation percentage. Best estimates of geometric rates of return for each major asset class included in the Pension Reserve Investment Trust (PRIT) Fund's target allocation as of June 30, 2018 are summarized in the following table:

<u>Asset class</u>	<u>Target allocation</u>	<u>Long term expected real rate of return</u>
Core fixed income	12 %	0.9 %
Value added fixed income	10	3.8
Global equity	39	5.0
Real estate	10	3.8
Private equity	12	6.6
Portfolio completion strategies	13	3.7
Timber/natural resources	4	3.4
Total	<u>100 %</u>	

(e) Discount Rate

The discount rate used to measure the total pension liability was 7.35%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that contributions will be made at contractually required rates, actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

(i) *Pension Plan Fiduciary Net Position*

Detailed information about the pension plan's fiduciary net position is available in the Commonwealth's financial report.

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(8) Other Post-Employment Benefits (OPEB)

(a) Plan Description

The Health Connector administers a single-employer defined benefit OPEB plan. The plan provides post-employment health care and life insurance benefits (OPEB) for eligible retired employees through the Group Insurance Commission (GIC). The GIC administers and manages health coverage options and benefits to participating employees and retirees. As of January 1, 2017, the date used for actuarial census data, the Health Connector had two retirees and 65 active employees who met the eligibility requirements. No assets are accumulated in a trust that meets the criteria of paragraph 4 of Statement No. 75.

(b) Benefits Provided

The Health Connector provides medical, dental, prescription drug, mental health/substance abuse and life insurance to retirees and their covered dependents. All active employees who retire from the Health Connector and meet the eligibility criteria will receive these benefits.

(c) Contributions

Employees who retire after July 1, 1994 but on or before October 1, 2009 contribute 15% of the cost of the health plan, as determined by the GIC. Employees who retire after October 1, 2009 contribute 20% of the cost of the plan as determined by the GIC. In both cases, the Health Connector contributes the remainder of the health plan costs on a pay-as-you-go basis.

(d) Total OPEB Liability

The Health Connectors' total OPEB liability of \$6,176,965 was measured as of June 30, 2018 and was determined by an actuarial valuation as of January 1, 2017 rolled forward to June 30, 2018.

(i) Actuarial Assumptions and Other Inputs

The total OPEB liability as of June 30, 2018 was determined using the following actuarial assumptions and other inputs, applied to all periods included in the measurement period:

Inflation	3.0 percent
Salary Increases	4.5 percent, average, including inflation
Healthcare cost trend rates	8.0 percent for 2018, decreasing 0.5 percent per year to an ultimate rate of 5.0 percent for 2024 and later years
Actuarial cost method	Entry age normal with 30 year open amortization period

Pre-retirement mortality reflects PUB-2010 Headcount-Weighted General Classification Employee and Healthy Annuitant table projection generationally with Scale MP-2018.

Post-retirement mortality reflects PUB-2010 Headcount-Weighted General Classification Employee and Healthy Annuitant table projection generationally with Scale MP-2018.

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For disabled members, the mortality rate reflects PUB-2010 Headcount-Weighted General Classification Employee and Healthy Annuitant table projection generationally with Scale MP-2018.

(ii) *Discount Rate*

The discount rate used to measure the total OPEB liability as of June 30, 2019 was 3.87% an increase from the prior year discount rate of 3.58%. The discount rate is based on the Bond Buyer General Obligation 20-year Municipal Bond Index, which includes tax-exempt general municipal bonds with an average rating of AA/Aa or higher.

Changes in Total OPEB Liability	
Balance at June 30, 2018	\$ 5,601,661
Changes for the year:	
Service cost	711,299
Interest on the total OPEB liability	225,939
Differences between expected and actual experiences	(51,916)
Change of assumptions	(306,354)
Benefit payments	<u>(3,664)</u>
Net changes	<u>575,304</u>
Balance at June 30, 2019	<u>\$ 6,176,965</u>

Change of assumptions reflect a change in the discount rate from 3.58% to 3.87% in 2019, and the mortality assumption was updated from the RP-2014 Blue Collar Employees and Healthy Annuitant tables projected generationally with scale MP-2016, set forward 1 year for females, to PUB-2010 Headcount-weighted General Classification Employee and Healthy Annuitant tables projected generationally with Scale MP-2018 for all participants.

(iii) *Sensitivity of the Total OPEB Liability to Changes in the Discount Rate and Healthcare Cost Trend Rates*

The following table presents the total OPEB liability of the Health Connector, as well as what the Health Connector's total OPEB liability would be if it were calculated using a discount rate that is 1-percentage-point lower (2.87%) or 1-percentage-point higher (4.87%) than the current discount rate:

	1% Decrease (2.87%)	Discount rate (3.87%)	1% Increase (4.87%)
Total OPEB liability	\$ 7,866,749	6,176,965	4,927,606

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June 30, 2019

The following table presents the total OPEB liability of the Health Connector, as well as what the Health Connector's total OPEB liability would be if it were calculated using healthcare cost trend rates that are 1-percentage-point lower or 1-percentage-point higher than the current healthcare cost trend rates:

	(7.5% decreasing to 4.0%) 1% decrease	Current healthcare cost trend rate – 8.5% decreasing to 5.0%	(9.5% decreasing to 6.0%) 1% increase
Total OPEB liability	\$ 4,510,769	6,176,965	8,688,251

(e) OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

For the year ended June 30, 2019, the Health Connector recognized OPEB expense of \$627,824. The following table illustrates the Deferred Inflows as of June 30, 2019 under GASB 75.

	Deferred inflows
Difference between actual and expected experience	\$ 48,015
Assumption changes	<u>3,450,868</u>
Total deferred inflows	<u>\$ 3,498,883</u>

Amounts recognized in the deferred inflows of resources related to OPEB will be recognized in the OPEB expense as follows:

Year end June 30:	
2020	\$ (305,750)
2021	(305,750)
2022	(305,750)
2023	(305,750)
2024	(305,750)
Total thereafter	<u>(1,970,133)</u>
	<u>\$ (3,498,883)</u>

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(9) Operating Lease

The Health Connector has an operating lease for office space on three floors at 100 City Hall Plaza. The lease terminates on August 30, 2021. Future minimum operating lease payments at June 30, 2019 are as follows:

Fiscal year:		
2020	\$	723,373
2021		742,493
2022		<u>124,280</u>
	\$	<u><u>1,590,146</u></u>

During FY2019, the amount of operating lease payments was \$704,253.

(10) Capital Assets

Capital assets as of June 30, 2019 are as follows:

	<u>Ending balance June 30, 2018</u>	<u>Increases/ decreases</u>	<u>Ending balance June 30, 2019</u>
Capital assets not being depreciated:			
Computer software	\$ —	1,597,598	<u>1,597,598</u>
Total capital assets not being depreciated	<u>—</u>	<u>1,597,598</u>	<u>1,597,598</u>
Other capital assets:			
Computers and equipment	102,484	—	102,484
Furniture and fixtures	267,669	—	267,669
Computer software	<u>813,738</u>	<u>—</u>	<u>813,738</u>
Total other capital assets	<u>1,183,891</u>	<u>—</u>	<u>1,183,891</u>
Total capital assets	<u>1,183,891</u>	<u>1,597,598</u>	<u>2,781,489</u>
Less accumulated depreciation:			
Computers and equipment	(83,113)	(14,640)	(97,753)
Furniture and fixtures	(266,099)	(1,570)	(267,669)
Computer software	<u>(588,439)</u>	<u>(90,120)</u>	<u>(678,559)</u>
Total accumulated depreciation	<u>(937,651)</u>	<u>(106,330)</u>	<u>(1,043,981)</u>
Total capital assets, net	\$ <u>246,240</u>	<u>1,491,268</u>	<u>1,737,508</u>

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GASB Statement No.51 is a standard that characterizes an intangible asset as an asset that lacks physical structure, is nonfinancial in nature, and has an initial life expectancy beyond a single reporting period. Specific to the Health Connector in FY2019, \$1,597,598 in internally generated software costs were capitalized.

(11) State Funded Federal Replacement Cost Sharing Reduction Subsidy

In October 2017, the federal government discontinued federal CSR payments to the carriers for subsidized individuals as of September 2017. To ease the burden on the carriers, the Commonwealth made the decision to make state-funded federal replacement cost sharing reduction subsidy payments to the carriers for the period October 2017 through December 2017. These state funded payments were based on monthly premium data and was subject to reconciliation based on the final actual claims data submitted by the carriers in 2019. As a result, \$1,853,425 was due to the carriers in FY2019.

(12) Commitments and Contingencies

The Health Connector is involved in legal actions arising in the normal course of activities. Although the ultimate outcome of such matters is not determinable at this time, management, after taking into consideration advice of legal counsel, believes that the resolutions of pending matters will not have a materially adverse effect, individually or in the aggregate, upon the Health Connector's financial statement.

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Schedule of Proportionate Share of Net Pension Liability
Required Supplementary Information

June 30, 2019

(Unaudited)

	2019	2018	2017	2016
	(measurement	measurement	(measurement	(measurement
	date	date	date	date
	June 30, 2018)	June 30, 2017)	June 30, 2016)	June 30, 2015)
Health Connector's proportion of the net pension liability	0.11708 %	0.11645 %	0.11441 %	0.10439 %
Health Connector's share of the net pension liability	\$ —	—	—	—
State's proportionate share of the net pension liability associated with the Health Connector	<u>15,489,168</u>	<u>14,934,603</u>	<u>15,775,710</u>	<u>11,882,332</u>
Total net pension liability	\$ <u>15,489,168</u>	<u>14,934,603</u>	<u>15,775,710</u>	<u>11,882,332</u>
Health Connector's covered-employee payroll	\$ 7,064,044	6,649,289	6,286,232	5,860,359
Health Connector's proportionate share of the net pension liability as a percentage of its covered-employee payroll	— %	— %	— %	— %
Plan fiduciary net position as a percentage of the total pension liability	67.91 %	67.21 %	63.50 %	67.90 %

The Health Connector is not required to make contributions to the State Employees Retirement System.

Accordingly, the RSI related to statutorily or contractually contributions is not presented.

Note: This schedule is intended to present 10 years of data. Additional years will be presented when available.

See accompanying independent auditors' report.

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Schedule of Changes in Total OPEB Liability and Related Ratios

June 30, 2019

(Unaudited)

	2019	2018
	(measurement	(measurement
	date	date
	<u>June 30, 2018)</u>	<u>June 30, 2017)</u>
Total OPEB liability:		
Service cost	\$ 711,299	1,215,462
Interest on the total OPEB liability	225,939	258,534
Differences between expected and actual experiences	(51,916)	—
Change of assumptions	(306,354)	(3,725,195)
Benefit payments	<u>(3,664)</u>	<u>(6,057)</u>
Net change in total liability	575,304	(2,257,256)
Total OPEB liability – beginning	<u>5,601,661</u>	<u>7,858,917</u>
Total OPEB liability – ending	\$ <u><u>6,176,965</u></u>	\$ <u><u>5,601,661</u></u>
Fiduciary net position as a percentage of OPEB liability	\$ —	—
Covered-employee payroll	7,064,044	6,649,289
Net OPEB liability as a percentage of covered-employee payroll	87 %	84 %

Notes to schedule:

2018

Changes of Assumptions:

The discount rate was changed from 3.58% as of the June 30, 2017 measurement date to 3.87% as of the June 30, 2018 measurement date.

The mortality assumption was updated from the RP-2014 Blue Collar Employees and Healthy Annuitant tables projected generationally, with scale MP-2016, set forward 1 year for females, to PUB-2010 Headcount-weighted General Classification Employee and Healthy Annuitant tables projected generationally with Scale MP-2018 for all participants.

2017

Changes of Assumptions:

The discount rate was changed from 2.85% as of the June 30, 2016 measurement date to 3.58% as of the June 30, 2017 measurement date.

Note: This schedule is intended to present 10 years of data. Additional years will be presented when available.

See accompanying independent auditors' report.